

**ANALYSIS OF DIVISION OF COMPLIANCE AND CONSUMER
AFFAIRS' 1999 EXAMINATION WORKLOAD**

Audit Report No. 99-042
September 30, 1999

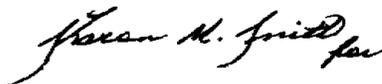


OFFICE OF AUDITS

OFFICE OF INSPECTOR GENERAL

DATE: September 30, 1999

TO: Stephen M. Cross, Director
Division of Compliance and Consumer Affairs



FROM: David H. Loewenstein
Assistant Inspector General

SUBJECT *Analysis of Division of Compliance and Consumer Affairs' 1999 Examination Workload (Audit Report No. 99-042)*

The Federal Deposit Insurance Corporation (FDIC) Office of Inspector General (OIG) has completed a review to determine how the Division of Compliance and Consumer Affairs (DCA) planned to achieve its 1999 examination workload requirements with its given resource levels. The downsizing of the FDIC workforce, combined with changes in DCA's examination frequency policy and the training of new and crossover employees, led the OIG to examine DCA's ability to conduct all of the compliance and Community Reinvestment Act (CRA) examinations scheduled for calendar year 1999.

As of December 31, 1998, there were 523 compliance/CRA examination delinquencies that were carried over into the 1999 workload. According to DCA management, the FDIC Chairman has mandated that DCA will conduct all compliance/CRA examinations and visitations scheduled for 1999, including the 1998 delinquencies. The goal of this audit was to determine if DCA, given the current level of resources, can accomplish its compliance/CRA examination and visitation workload. The OIG will continue to monitor DCA's progress in meeting their workload objectives for the remainder of 1999 and provide interim status reports as needed. In addition to evaluating the DCA workload and staffing resources, we did observe a separate issue that we believe should be brought to FDIC and DCA management's attention.

BACKGROUND

The 1998-2003 FDIC Strategic Plan provides a framework for implementing the agency's mission by setting a course for the organization and guiding decisions about the effective use of resources. The FDIC Strategic Plan is implemented through the Corporate Annual Performance Plan, which is augmented by individual division and office plans from which staffing and budget resources are determined.

We focused on DCA's strategic goal of evaluating the compliance of FDIC-supervised institutions with consumer protection and fair lending laws and their performance under CRA. The FDIC's primary means of accomplishing its goal to ensure compliance with consumer protection is through bank compliance examinations. Noncompliance with consumer protection laws may result in corrective enforcement actions requiring payment of restitution or penalties, or reimbursement to customers of improperly charged fees or interest. As required by CRA, DCA also periodically evaluates each institution's record of helping to meet its community's

credit needs.

Congress, by statute, has assigned the FDIC enforcement responsibilities for various consumer protections, civil rights and certain other regulations for state chartered, non-member financial institutions supervised by the FDIC. Some of the more prominent laws and regulations include the Truth in Lending Act, the Fair Credit Reporting Act, the Real Estate Settlement Procedures Act, the Fair Housing Act, and the Home Mortgage Disclosure Act. In addition, the Community Reinvestment Act of 1977 encourages each covered financial institution insured by the FDIC to participate in meeting the needs of the communities in which it operates. The CRA also requires that each federal financial supervisory agency assess the record of each covered depository institution in helping to meet the credit needs of its community (including low- and moderate-income neighborhoods) while staying consistent with safe and sound operations and that the appropriate supervisory agency take that record into account when deciding whether to approve an application by the institution for a deposit facility.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objective of the audit was to determine if DCA, given its current level of resources, can accomplish its 1999 compliance/CRA examination and visitation workload. To accomplish this objective, we: (1) interviewed DCA management to discuss the workload planning process; (2) interviewed the Division of Administration's Associate Director, Management Review, to discuss DCA's core staffing process; (3) reviewed DCA's performance plans and quarterly reports indicating the level of performance actually attained; (4) reviewed DCA's core staffing projections; (5) reviewed published CRA examination schedules and compared these schedules to the actual CRA examinations conducted; and (6) analyzed and estimated the number of hours required to accomplish the Chairman's goal and other DCA examination activities for 1999.

Fieldwork was performed exclusively in Washington, D.C. The audit was conducted in accordance with generally accepted government auditing standards for performance audits. We conducted the audit from February 1999 to August 1999.

We have relied on core staffing information provided by DCA. The core staffing data was independently analyzed by the FDIC's Division of Administration and subsequently approved by the FDIC's Board of Directors in conjunction with their approval of the FDIC's 1999 annual budget. In addition, we have relied on information generated from DCA's Compliance Statistical System (CSS) and the Scheduling, Hours, and Reporting Package (SHARP) system; however, we have not tested or verified the reliability of these systems.

RESULTS OF AUDIT

Based on our review of DCA's 1999 estimated workload, we believe DCA can accomplish its 1999 examination workload requirements. Assuming that there will be no major unscheduled events during 1999, we believe that DCA will be able to fulfill the FDIC Chairman's mandate that all 1999 scheduled compliance/CRA examinations and visitations, including 1998 delinquencies, be conducted as of the year's end.

During this review, we also observed 103 instances for 1998 and 130 instances for the first quarter of 1999 in which CRA examinations were not included in the appropriate advance quarterly schedule, which is used to provide written public notification as required by the CRA regulation. As a result, the FDIC has not afforded community groups the opportunity to provide timely comments on each of these banks' performance.

Analysis of DCA's 1999 Examination Workload

The FDIC Chairman mandated that DCA conduct all 1999 regularly scheduled compliance/CRA examinations, the 1998 delinquent examinations, and visitations by year-end 1999. According to DCA officials, the Chairman's mandate was not written, but expressed verbally to DCA management. Our review indicates that DCA management has taken the necessary steps to shift workload priorities so that they can conduct the examinations scheduled in 1999 as well as the 1998 delinquent examinations. DCA management has reduced examiner training by approximately 50 percent for calendar year 1999.

As part of our analysis, we calculated the projected DCA examiner hours available and compared them to estimated hours needed for examiners to conduct the compliance/CRA examinations and visitations¹ for calendar year 1999 (see table 1 below).

TABLE 1

Analysis of DCA's Ability to Conduct Compliance/CRA Examination and Visitation Workload Scheduled For 1999

Projected Hours Available to Conduct Examinations in 1999	
398.5 (Examiners on Board) x 1,100* (Hrs. Avail. Per Examiner)	438,350
Less: Hours Needed to Conduct 1999 Workload**	
Hours to Conduct 1998 Compliance/CRA Examination Delinquencies (176 average hours x 523 examinations)	-92,048
Hours to Conduct 1999 Compliance/CRA Examination Workload (176 average hours x 1,792 examinations)	-315,392
Hours to Conduct 1999 Projected Visitation Workload (75 average hours x 240 projected visitations)	-18,000
Total Remaining Examination Hours Available	<u>12,910</u>

Source: OIG Analysis / Division of Compliance and Consumer Affairs

*The number of annual hours available per examiner to conduct compliance/CRA examinations and visitations. The 1,100 hours is based on a total of 2,080 annual staff hours available per examiner.

**The average hours needed to conduct compliance/CRA examinations scheduled in 1999 were based on the actual average hours needed to complete examinations in 1998. These hours were then multiplied by the number of examinations scheduled for 1999, including delinquent examinations from 1998.

¹ Visitations are a means for the FDIC to ascertain the compliance posture or implementation of corrective procedures without conducting a full compliance examination. Visitations are usually targeted to specific areas previously identified as weak.

Our analysis indicates that DCA has a sufficient number of examiner hours available to initiate all 2,315 compliance/CRA examinations scheduled to be started in 1999, and its projected 240 visitations. This analysis is based on DCA's 1998 actual average of 176 hours per examination. Our conclusion that DCA has sufficient hours to conduct its workload assumes that DCA examiners will maintain this level of efficiency during 1999. DCA management told us that its examiners have become more experienced and the average time to complete an examination is declining. Because of these trends, DCA officials informed us that DCA management requested that the average examination hours per million dollars of total bank assets be reduced by 20 percent.

DCA has projected that the 1999 compliance/CRA examinations will take an average of 186 hours to complete. According to DCA officials, the 1999 estimated average hours is higher than the actual 1998 average hours because DCA has scheduled more reviews of larger banks in 1999. If DCA's estimate of 186 average hours to complete the 1999 compliance/CRA examinations is accurate, there would be a shortage of 10,240 hours needed to conduct the 2,315 scheduled compliance/CRA examinations and the 240 projected visitations. However, on September 29, 1999, DCA provided us with the actual average hours expended as of September 1, 1999 for compliance/CRA examinations initiated within the first two quarters of 1999. According to that data, there were 1,363 compliance/CRA examinations started between January 1, 1999 and June 30, 1999 with the total hours per examination averaging 169 hours.² We believe this data more closely aligns with the 176 average hours per examination we used in our analysis, as opposed to the 186 hours projected by DCA.

Our review of DCA's 1999 first and second quarter examination activities indicates that DCA started 118 more examinations than projected for the first two quarters of 1999. DCA had started 1,363 examinations from January 1, 1999 through June 30, 1999, or 59 percent of the 2,315 examinations scheduled to be started during 1999. As of June 30, 1999, a total of 211,415 hours, or approximately 48 percent of the projected hours available to conduct compliance/CRA examinations and visitations, had been expended. In addition, as of June 30, 1999, 101 visitations had been conducted. DCA officials stated that the actual number of examinations started during the first two quarters of 1999 may not be representative of the examination starts in the subsequent quarters of 1999. They indicated that more annual leave is typically taken during the summer months and the year-end holiday seasons. As a result, an increase in the use of annual leave may cause the number of examination starts to decline in later quarters of the year.

Our review of examiner hours available for examinations and our assessment of the examination hours used in the first two quarters of 1999 indicate that DCA is on track to accomplish their 1999 workload. We plan to continue to monitor and evaluate DCA's progress in accomplishing the workload scheduled for the remainder of 1999.

As a result of this review, we have also identified an issue regarding the oversight of the CRA workload. The following section addresses this issue and our recommendations.

² As of September 1, 1999, 55 of the 1,363 compliance/CRA examinations started from January 1, 1999 through June 30, 1999 were still in process. Therefore, the actual average hours per examination should increase slightly.

DCA Has Provided Inaccurate Notification of Planned CRA Examinations

DCA is required by regulation (12 CFR, Part 345.45) to publish quarterly public notices of planned CRA examinations in order to provide individual consumers and consumer groups an opportunity to comment on bank performance for DCA's consideration during CRA examinations. However, we found that a total of 233 CRA examinations were initiated during 1998 and the first quarter of 1999 without being included in the appropriate quarterly schedule.

As of January 1, 1996, the regulation requires that the FDIC publish "at least 30 days in advance of the beginning of each calendar quarter a list of banks scheduled for CRA examinations in that quarter." This publication is required to encourage public comment on the institutions to be examined under CRA. Public comments that are received before the close of the CRA examination will be considered by the DCA examiners.

FDIC press releases contain a statement that the examination schedule is based on the best information available, but that the examination schedule is subject to change. In addition, the statement informs the public that under some circumstances, conditions may arise where an unanticipated examination may take place without inclusion on the published list. Circumstances that could cause an unanticipated examination may include a CRA protest, a consumer complaint, or some other significant event. The news release also states "If an institution is rescheduled for a different quarter, that information will be included on a later list."

We reviewed a list of examinations actually started in 1998 and the first quarter of 1999 to determine if all of these examinations had been properly advertised in advance. We found that 103 examinations were started in 1998 without being advertised to start in the corresponding quarter. We also found 130 examinations started in the first quarter of 1999 that were not advertised to be started in that quarter.

We performed a detailed analysis of the 130 examinations started in the first quarter of 1999 that had not been published for that quarter. We found that of the 130 examinations:

- 22 examinations were scheduled and advertised to be started in one of the last two quarters of 1998 but not re-advertised for the first quarter of 1999;
- 78 examinations were not advertised until the quarter after the examination was started; and
- 30 examinations were started but never included in a published CRA schedule of examinations.

We also found that the regional offices varied in their degree of compliance with the published schedule of CRA examinations for the first quarter of 1999. Table 2 summarizes the regional variances we found in compliance with the published schedule of examinations.

TABLE 2

**CRA Examinations Started in First Quarter 1999
Compared to Published CRA Examination Schedule**

<i>DCA Region</i>	<i>Total CRA Exams Started</i>	<i>Exams Not Published for the Quarter</i>	<i>% of Exceptions to Total CRA Exams Started</i>
<i>Atlanta</i>	68	5	7%
<i>Boston</i>	40	1	3%
<i>Chicago</i>	145	46	32%
<i>Dallas</i>	99	20	20%
<i>Kansas City</i>	208	23	11%
<i>Memphis</i>	100	26	26%
<i>New York</i>	47	0	0%
<i>San Francisco</i>	58	9	16%
<i>Totals</i>	765	130	17%

Source: OIG Analysis / DCA Data

Guidelines for preparing the quarterly list of scheduled CRA examinations were revised in July 1998 through the issuance of DCA Memorandum #98-014. These guidelines were first implemented for the preparation and publication of the fourth quarter 1998 CRA Examination Schedule. We believe our analysis indicates that these guidelines did not result in improvements to the quarterly scheduling of CRA examinations. However, starting with the publication of the second quarter 1999 CRA Examination Schedule, DCA extended the deadlines for the DCA regional offices to submit CRA examination schedules by approximately ten calendar days. This was done to further improve the accuracy of the published CRA examination schedules.

Although DCA has delegated responsibility for preparing the quarterly list of scheduled examinations to the regional directors, DCA headquarters has not monitored the accuracy of the advertised quarterly schedule of examinations. As a result, the FDIC has not afforded community groups the opportunity to provide timely comments on each of these banks' performance.

Recommendations

To ensure the published quarterly schedules provide consumers with the best opportunity to comment on bank performance, we recommend that the Director, DCA:

- (1) Establish a system of controls in regional and field offices to ensure the published quarterly schedule of CRA examinations is as accurate as possible,
- (2) Monitor regional office compliance with the published quarterly schedule of CRA examinations, and
- (3) Review the accuracy of regional office reporting on compliance with the published quarterly schedule of CRA examinations as part of the regional and field office internal control reviews.

CORPORATION COMMENTS AND OIG EVALUATION

On September 30, 1999, the Director, DCA, provided a written response to the draft report. The response is presented in appendix I to this report.

The Director, DCA, stated that he agreed with report recommendations 2 and 3 and will implement corrective action in the fourth quarter of 1999. With regards to recommendation 1, he does not envision that DCA needs additional procedural changes to ensure a more accurate published schedule of CRA examinations, and therefore does not agree that the recommendation is necessary. The Director stated that the high number of exceptions we identified in the first quarter of 1999 was due to an extraordinary year-end policy change that occurred after the publication of the first quarter 1999 examination schedule. The regions were directed to conduct more examinations in 1999 than originally planned and to place a priority on eliminating delinquent examinations. In addition, in the fourth quarter of 1998, DCA issued revised guidelines for preparing the quarterly list of scheduled CRA examinations.

We believe that the Director, DCA has provided a reasonable explanation for not needing additional controls to improve the accuracy of published quarterly CRA schedules. Also, by agreeing to implement recommendations 2 and 3, DCA will be monitoring the accuracy of the quarterly published schedules of CRA examinations and should detect if additional procedural changes are necessary. Therefore we concur with DCA's decision not to implement recommendation 1.

September 30, 1999

TO: Steven A. Switzer, Deputy Inspector General for Audits
Office of Inspector General



FROM: Stephen M. Cross, Director
Division of Compliance and Consumer Affairs

SUBJECT: Response to OIG Draft Report Entitled *Analysis of Division of Compliance and Consumer Affairs 1999 Examination Workload*

Thank you for the opportunity to comment on your report *Analysis of Division of Compliance and Consumer Affairs 1999 Examination Workload*. The report makes a number of valuable observations about our 1999 examination workload as well as recommendations regarding publishing CRA examination schedules.

Analysis of DCA's 1999 Examination Workload

We agree with your assessment that the examination hours used in the first two quarters of 1999 indicates that DCA is on track to accomplish their 1999 examination workload. We have provided comments to your staff, via e-mail and through discussions, clarifying items presented in the section. A copy of the comments and related documentation provided is attached.

Notification of Planned CRA Examinations

In your report you also make three recommendations about publishing CRA examination schedules.

1. Establish a system of controls in regional and field offices to ensure the published quarterly schedule of CRA examinations are as accurate as possible.
2. Monitor regional office compliance with the published quarterly schedule of CRA examinations.
3. Review the accuracy of regional office reporting on compliance with the published quarterly schedule of CRA examinations as part of the regional office and field office internal control reviews ("ICR").

Before addressing those three recommendations in detail, however, we would like to comment on the exceptions to the planned CRA schedule noted in your report. In addition to items noted in your report, there are other exigent business circumstances contributing to why the CRA publication time-frame and the actual examination start date are in different calendar quarters.

For example, in situations where an office has the opportunity of being able to start more examinations than it originally had planned for the quarter an examined bank will not have been published prior to the examination. In such circumstances we could actually list the bank on the next published list even though the examination will have already concluded or not published the bank's name at all. Neither seems an ideal solution, yet either option is an unavoidable "exception" under the criteria used in this report for identifying errors. Alternatively, if an examination is scheduled to start just before the end of the current quarter, it could be delayed until a few weeks into the next quarter. This could be considered an exception under the criteria used in this report, but is an understandable result of changing circumstances.

We are satisfied with the reliability of our 1998 published data. Your staff found 103 exceptions, which translates into a 5 percent error rate. Given the various uncontrollable and unpredictable circumstances that make examination scheduling difficult to forecast with precision, we believe an exception rate of roughly 5 percent to be reasonable.

The high number of exceptions (130) identified in the first quarter of 1999 is due to an extraordinary year-end policy change that occurred after the publication of the first quarter 1999 examination schedule. DCA Regional Directors were directed to make significant adjustments to their respective examination schedules in December 1998. Those changes occurred after the regions submitted their CRA examination schedules in late November for publication. The regions were directed to conduct more examinations in 1999 than originally planned and to place a priority on eliminating delinquent examinations. The regions with the most delinquent examinations going into 1999 were Chicago, Dallas, and Kansas City. Those regions, along with Memphis, accounted for most of the scheduling exceptions as illustrated in Table 2 of your report. The Memphis region's exception rate was high since they were unexpectedly assigned many of Chicago's delinquent banks in the first quarter, but had not included that group of banks on the first quarter published list. Given these circumstances, we believe the results of the first quarter of 1999 are an anomaly and that our 1998 published schedules are much more representative of our regions' ability to reasonably forecast future examinations.

Instances where unforeseen circumstances cause an examination to be conducted in the quarter following its published quarter are not "errors". The purpose of the published schedule is to inform the public providing them an opportunity to comment on a bank's record prior to its examination. The regulation anticipates that plans could change, but only calls for publication of planned examinations. In cases where an examination is delayed by just one quarter the public has in fact been recently notified of the upcoming examination and is afforded the opportunity to provide comments that will be forwarded to the field office for their review and consideration when the examination is conducted in the subsequent quarter. Therefore, headquarters staff has actually discouraged regions from re-publishing the same bank in successive quarters. However, if an examination is delayed longer than that, re-publishing the bank on a subsequent CRA examination list is considered appropriate.

Recommendation 1 – Establish a system of controls in regional and field offices to ensure the published quarterly schedule of CRA examinations are as accurate as possible.

The CRA quarterly schedules submitted by the regions are based on projections provided by the Field Office Supervisors. These individuals have the best information available to make a good-faith estimate of upcoming examination activity and serve as the division's most direct and reliable source for matters related to examination scheduling. In addition, DCA, in the fourth quarter 1998, has issued revised guidelines for preparing the quarterly list of scheduled CRA examinations. These guidelines provide the regions with two to three additional weeks before having to submit their scheduling plans.

With the Field Office Supervisors using these procedures to develop their best estimate of upcoming activities, we do not envision the need for additional procedural changes to ensure a more accurate schedule.

Recommendation 2 – Monitor regional office compliance with the published quarterly schedule of CRA examinations.

And

Recommendation 3 – Review the accuracy of regional office reporting on compliance with the published quarterly schedule of CRA examinations as part of the regional office and field office internal control reviews (“ICR”).

DCA concurs with the above recommendations. DCA's Washington Operations will evaluate the accuracy of the CRA examination schedule quarterly to ensure each region is maintaining a nominal exception rate. DCA's Washington Operations will prepare a report for distribution to Washington and Regional Management comparing the CRA examinations scheduled and published for a quarter with the examinations actually started during the quarter. For all CRA examinations that were performed during the quarter and were not published, we will require the regions to provide us with an explanation as to why the examinations were not published, and, if possible, the actions they will take to prevent such an error in the future. We plan to fully implement this procedure beginning with an evaluation of the fourth quarter 1999 CRA examination schedule.

APPENDIX II

MANAGEMENT RESPONSES TO RECOMMENDATIONS

The Inspector General Act of 1978, as amended, requires the OIG to report the status of management decisions on its recommendations in its semiannual reports to the Congress. To consider FDIC's responses as management decisions in accordance with the act and related guidance, several conditions are necessary. First, the response must describe for each recommendation

- the specific corrective actions already taken, if applicable;
- corrective actions to be taken together with the expected completion dates for their implementation; and
- documentation that will confirm completion of corrective actions.

If any recommendation identifies specific monetary benefits, FDIC management must state the amount agreed or disagreed with and the reasons for any disagreement. In the case of questioned costs, the amount FDIC plans to disallow must be included in management's response.

If management does not agree that a recommendation should be implemented, it must describe why the recommendation is not considered valid.

Second, the OIG must determine that management's descriptions of (1) the course of action already taken or proposed and (2) the documentation confirming completion of corrective actions are responsive to its recommendations.

This table presents the management responses that have been made on recommendations in our report and the status of management decisions. The information for management decisions is based on management's written response to our report.

Rec. Number	Corrective Action: Taken or Planned/Status	Expected Completion Date	Documentation That Will Confirm Final Action	Monetary Benefits	Management Decision: Yes or No
1	The DCA Director disagreed with the recommendation. He responded that the high number of exceptions the OIG identified in the first quarter of 1999 was due to an extraordinary year-end policy change that occurred after the publication of the first quarter 1999 examination schedule. The regions were directed to conduct more examinations in 1999 than originally planned and to place a priority on eliminating delinquent examinations. In addition, in the fourth quarter of 1998, DCA issued revised guidelines for preparing the quarterly list of scheduled CRA examinations. We believe that the Director, DCA has provided a reasonable explanation for not needing additional controls to improve the accuracy of published quarterly CRA schedules. Also, by agreeing to implement recommendations 2 and 3, DCA will be monitoring the accuracy of the quarterly published schedules of CRA examinations and should detect if additional procedural changes are necessary. Therefore we concur with DCA's decision not to implement recommendation 1.	N/A	N/A	N/A	Yes

Rec. Number	Corrective Action: Taken or Planned/Status	Expected Completion Date	Documentation That Will Confirm Final Action	Monetary Benefits	Management Decision: Yes or No
2	Response indicated agreement with the recommendation. DCA's Washington Operations will evaluate the accuracy of the CRA examination schedule quarterly to ensure each region is maintaining a nominal exception rate.	Fourth Quarter 1999	DCA Washington will issue a written report	Not Quantifiable	Yes
3	Response indicated agreement with the recommendation. DCA's Washington Operations will evaluate the accuracy of the CRA examination schedule quarterly to ensure each region is maintaining a nominal exception rate.	Fourth Quarter 1999	DCA Washington will issue a written report	Not Quantifiable	Yes